

General Information Letter: Nexus decision are not appropriately made in letter rulings.

October 9, 2001

Dear:

This is in response to your letter dated August 6, 2001 in which you state the following:

We are writing in regards to the above corporation, concerning their corporate taxable filing requirements.

It has come to our attention that the above corporation may not be required to file a corporate income tax return in your state. This is based on the following information:

1. The Company is a distributor of orthodontic products, which is based in xxxxxxxxx, Missouri.
2. All products are sold and shipped from the xxxxxxxxx office in Missouri.
3. They have one sales representative in your state to make phone calls to prospective customers (dentists) and distribute brochures, on their line of orthodontic products, to dental offices. The salesman does not provide any services. The salesman is only in your state to disburse information about the Company's products.
4. The salesman can take an order and fax it for the customer; but, most orders are either called, faxed or E-mailed to the xxxxxxxxx office in Missouri directly by the customers (dental offices).
5. All orders are approved and finalized at the xxxxxxxxx office.
6. Any returns, exchanges or adjustments are handled through contact with the xxxxxxxxx office, not by the salesman. If the salesman is called first, about any of these issues, he refers them to the xxxxxxxxx office.
7. There is no training required in the use of the orthodontic products, because the dentists already know how to use the products this Company sells.
8. The salesman carries a sample case of the products, but none of it is available for sale.

Since this Company has no business activity in your state, other than sales, we would like a rendering as to the corporate tax requirements of this Company. They are set up with the withholding and unemployment tax departments to report the payroll paid to the employee. We know that those tax responsibilities will continue, no matter what the ruling is on the corporate tax issue.

We feel this Company should only have to file a state income tax return for the state of Missouri, showing all sales as Missouri based. However, we would appreciate your guidance in this matter.

According to the Department of Revenue ("Department") regulations, the Department may issue only two types of letter rulings: Private Letter Rulings ("PLR") and General Information Letters ("GIL"). The regulations explaining these two types of rulings issued by the Department can be found in 2 Ill. Adm. Code §1200, or on the website <http://www.revenue.state.il.us/legalinformation/regs/part1200>.

Due to the nature of your inquiry and the information presented in your letter, we are required to respond with a GIL. GILs are designed to provide background information on specific topics. GILs, however, are not binding on the Department.

Section 201 of the Illinois Income Tax Act ("IITA"), 35 ILCS 5/101 et seq, imposes a tax measured by net income on corporations for the privilege of earning or receiving income in this State. The Due Process and Commerce Clauses of the Federal Constitution limit the power of States to subject foreign corporations to tax. The Due Process Clause requires that there exist some minimum connection between a state and the person, property, or transaction it seeks to tax (Quill Corp. v. North Dakota, 504 U.S. 298, 112 S.Ct. 1904 (1992)). Similarly, the Commerce Clause requires that the tax be applied to an activity with a substantial nexus with the taxing state. Id.

Unless protected by Public Law 86-272, a foreign corporation has the requisite nexus to subject it to Illinois income tax where any part of its income is allocable to Illinois in accordance with the provisions of Article 3 of the Illinois Income Tax Act (35 ILCS 5/301-304, 308). Public Law 86-272 is a federal statute that prohibits a state's taxation of interstate sales of tangible personal property.

Your letter indicates that xxxxxxxxxxxxxxxxxxxxxxxx (hereinafter "xxxxxxxxxxxxx") has a full time employee in Illinois who acts as a salesman for the corporation. Although your letter mentions selling "orthodontic products" in the state of Illinois, we cannot ascertain whether xxxxxxxxxxxxx only sells products classified as tangible personal property. If yes, xxxxxxxxxxxxx may be protected under Public Law 86-272. However, if xxxxxxxxxxxxx is not in the business of selling tangible personal property, it would not be protected by Public Law 86-272.

The courts have determined that occasional visits to another state would probably satisfy the commerce and due process clauses. For example, in the New York case of Orvis v. Tax Appeals Tribunal, 86 N.Y.2d 165, 654 N.E.2d 954 (1995), the court found that four visits to nineteen customers in one year was enough to allow the state to tax a Vermont wholesaler. In your situation, xxxxxxxxxxxxx has a full time employee acting as a salesman in Illinois. Such a regular act of gaining sales throughout the state of Illinois may give rise to the requisite nexus to subject xxxxxxxxxxxxx to Illinois Income tax. The income from these Illinois sales may be allocable to Illinois in accordance with provisions of Article of the IITA.

If a corporation does establish nexus, business income will be apportioned to Illinois under Section 304 of the IITA. Illinois uses a single-sales factor approach that looks at the amount of money that is retrieved from Illinois compared to the amount retrieved from all other states.

The question of nexus is highly fact-dependent. Therefore, the Department does not issue rulings regarding whether a taxpayer has nexus with the State. Such a determination can only be made in the context of an audit where a Department auditor has access to all relevant facts and circumstances.

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As stated above, this is a general information letter which does not constitute a statement of policy that either applies, interprets or prescribes tax law. It is not binding on the Department.

Sincerely,

Heidi S. Scott
Staff Attorney – Income Tax